

ORIGINAL



0000054956

MEMORANDUM

2006 JUN 21 P 2: 36

30

TO: Docket Control

FROM: Ernest G. Johnson
Director
Utilities Division

EA for EGJ

AZ CORP COMMISSION
DOCUMENT CONTROL

THRU: Matthew Rowell
Chief, Telecommunications and Energy Section
Utilities Division

DATE: June 23, 2006

RE: IN THE MATTER OF THE JOINT APPLICATION OF COMTEL TELCOM
ASSETS LP, VARTEC TELECOM, INC., EXCEL
TELECOMMUNICATIONS, INC. AND VARTEC SOLUTIONS, INC. FOR
APPROVAL OF A TRANSFER OF ASSETS (DOCKET NOS. T-20423A-05-
0677, T-03401A-05-0677, T-02584A-05-0677 AND T-03188A-05-0677)

Attached is the Staff Report on the Joint Application of Comtel Telcom Assets LP, VarTec Telecom, Inc., Excel Telecommunications, Inc. and VarTec Solutions, Inc. for approval of a transfer of assets. Staff recommends approval of the application

EGJ:WMS:red

Originator: Wilfred Shand, Jr.

Attachment: Original and Sixteen Copies

Service List for: Comtel Telcom Assets LP, VarTec Telecom, Inc., Excel Telecommunications, Inc. and VarTec Solutions, Inc.

Docket Nos. T-20423A-05-0677, T-03401A-05-0677, T-02584A-05-0677 and T-03188A-05-0677

Ms. Becky Gipson
Director Regulatory Affairs
VarTec Telecom, Inc.
2440 Marsh Lane
Carrollton, Texas 75006

Mr. Jeffery Crockett
Snell & Wilmer
One Arizona Center
400 East Van Buren
Phoenix, Arizona 85004-2202

Mr. Ernest G. Johnson
Director, Utilities Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Mr. Christopher C. Kempley
Chief Legal Counsel, Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Ms. Lyn Farmer
Chief Administrative Law Judge, Hearing Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

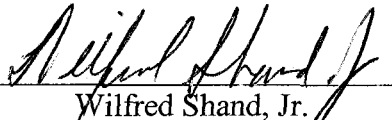
COMTEL TELCOM ASSETS LP, VARTEC TELECOM, INC., EXCEL
TELECOMMUNICATIONS, INC. AND VARTEC SOLUTIONS, INC.
DOCKET NOS. T-20423A-05-0677, T-03401A-05-0677, T-02584A-05-0677
AND T-03188A-05-0677

IN THE MATTER OF THE JOINT APPLICATION OF COMTEL TELCOM ASSETS LP,
VARTEC TELECOM, INC., EXCEL TELECOMMUNICATIONS, INC. AND VARTEC
SOLUTIONS, INC. FOR APPROVAL OF A TRANSFER OF ASSETS

June 23, 2006

STAFF ACKNOWLEDGEMENT

The Staff Report for the Joint Application of Comtel Telecom Assets LP, Vartec Telecom, Inc., Excel Telecommunications, Inc. and Vartec Solutions, Inc. For Approval of a Transfer of Assets (Docket Nos.T-20423A-05-0677, T-03401A-05-0677, T-02584A-05-0677 and T-03188A-05-0677), was the responsibility of the staff member listed below. Wilfred Shand, Jr. was responsible for the review and analysis of the application.

A handwritten signature in cursive script, appearing to read "Wilfred Shand, Jr.", is written over a horizontal line.

Wilfred Shand, Jr.
Public Utilities Analyst Manager

Introduction

On September 23, 2005, Comtel Telcom Assets LP ("Comtel") and VarTec Telecom, Inc., Excel Telecommunications, Inc., and VarTec Solutions, Inc. ("VarTec", "Excel" and "VarTec Solutions", respectively and the "VarTec Companies", collectively) submitted an application for Arizona Corporation Commission ("Commission") approval of the acquisition of certain of the VarTec Companies' assets by Comtel. The Applicants filed a Supplement to the application. The purpose of the Supplement is to provide additional information to support Comtel's application for a Certificate of Convenience and Necessity ("CC&N"). In addition the supplement is intended to clarify that applicants have no assets in Arizona and that this transaction is essentially a transfer of customers from the VarTec companies to Comtel.

The Parties

Comtel is a limited partnership organized under the laws of the State of Texas. Comtel is a newly formed limited partnership whose principal business will be telecommunications. Its general partner, Comtel Assets Inc. ("Comtel Inc.") owns 1 percent of the equity of Comtel. Comtel's limited partner, Comtel Assets Corp. ("Comtel Corp."), owns 99 percent of the equity of Comtel.

VarTec and Excel are corporations organized under the laws of the State of Texas. VarTec Solutions, which formerly operated under the corporate names, eMeritus Communications, Inc., Teleglobe Business Solutions, Inc. and Telco Holdings, Inc. d/b/a Dial & Save, is a Delaware corporation.

The VarTec Companies are privately-held corporations. VarTec Telecom Holding Company ("VarTec Holding"), a wholly-owned subsidiary of VarTec, holds 100 percent of the stock of Excelcom, Inc. ("Excelcom") and Telco Communications Group, Inc. ("Telco"). Excelcom is the direct and sole shareholder of Excel, and Telco is the direct and sole shareholder of VarTec Solutions. VarTec Holding and Excelcom are Delaware corporations, and Telco is organized in Virginia.

VarTec and Excel are certificated to provide competitive local exchange and interexchange services in Arizona. Specifically, VarTec was authorized by the Commission to provide competitive intraLATA and interLATA resold telecommunications services in Decision No. 62238 and was authorized to provide competitive facilities-based and resold local exchange and exchange access telecommunications services in Decision No. 65203. Excel was granted the authority to provide resold interexchange telecommunications services and competitive facilities-based and resold local exchange services in Decision No. 65470. VarTec Solutions was also authorized by the Commission to provide competitive resold interexchange telecommunications services in Decision No. 66640 under its former corporate name, eMeritus Communications, Inc.

The VarTec Companies voluntarily filed for Chapter 11 bankruptcy on November 1, 2004. As part of the bankruptcy process, the VarTec Companies have entered into an asset purchase agreement with Comtel Investments LLC ("Comtel Investments"). Comtel Investments, which is wholly owned by the same parties who own and control Comtel, has assigned its rights and obligations under the asset purchase agreement to Comtel as of August 1, 2005. The asset purchase agreement was executed on July 25, 2005, and was approved by the Court on July 27, 2005.

The Transaction

The VarTec Companies are operating under bankruptcy protection. Through the APA and the Court-approved auction process, Comtel will ultimately acquire substantially all of the assets of the VarTec Companies. In addition, Comtel currently intends to obtain up to approximately \$20 to \$25 million in debt financing pending consummation of the proposed transaction to fund working capital and similar needs of the VarTec Companies. Upon consummation of the proposed transaction, Comtel currently intends to replace such debt financing with a term (3 to 5 year) debt instrument. Based on Comtel's present understanding of the business, it anticipates that the term debt will be approximately \$50 million. This financing will assist with the day-to-day operations of Comtel as Comtel consummates its acquisition of the former VarTec Companies' operations, newly emerged from bankruptcy.

It is Comtel's understanding that once the proposed transaction is completed, the VarTec Companies will no longer hold authorizations to provide telecommunications services. These authorizations would be held by or assigned collectively to Comtel in order that Comtel can step into the shoes of the VarTec Companies, and the residential and commercial customers previously served by the VarTec Companies would continue to receive services without interruption. According to Comtel's initial plans for the business, the services provided and geographic areas served by Comtel will mirror those currently provided by the VarTec Companies, and any enhancements to the service offerings will be within the existing authority transferred to Comtel from the VarTec Companies. In order to minimize confusion and concern for customers, Comtel aims to make this transition seamless by operating under trade names and limiting all direct impacts to existing customers (e.g., no service changes are contemplated as part of this Application).

The applicants expect that the interconnection and other network agreements currently allowing the VarTec Companies to provide local exchange and/or interexchange services will be transferred to Comtel, as necessary, to continue the Applicants' efforts to make a smooth transition for customers. Comtel also initially plans to maintain the VarTec Companies' existing tariffs on file with the Commission. Once the transaction is prepared for closing and the Commission has granted its approval, Comtel will simply modify the corporate name on the tariffs.

Request for Approval to Transfer Assets

Comtel requests that the Commission approve the transfer of assets and simultaneously grant Comtel specific authority to operate as a provider of competitive resold interexchange and competitive facilities-based and resold local exchange and exchange access telecommunications services within Arizona. Specifically, Comtel requests that the Commission-issued CC&N be transferred from the VarTec Companies to Comtel. Comtel requests that new CC&Ns be issued if the Commission requires that new CC&Ns be issued. Comtel provided information in its application that it believes is typically required of new applicants seeking authorization to provide telecommunications services.

In addition, Comtel requests the authority to provide any and all of its services under the trade names VarTec Telecom, Clear Choice Communications, Excel Telecommunications and VarTec Solutions, in addition to the Comtel name. Comtel believes that this will maximize Comtel's available options under which it may begin its operations in the state.

Comtel will be led by a combination of its own management members and certain members of the existing management team of the VarTec Companies, who are currently expected to continue in management roles for Comtel after completion of the transaction. The five management members identified by the Applicants have a combined 80 years experience in the telecommunications industry. According to Comtel, the Federal Communications Commission has issued its approval for this transaction.

Financial Information

The Applicant provided unaudited financial statements for Comtel Telcom Assets, LP for the period July 19, 2006 through September 15, 2005. Comtel was formed in July 2005 and it has yet to begin operations. These financial statements list assets of \$43.5 million and Partner's Capital of \$43.5 million. Upon final closing, the partnership is to pay the seller \$40.5 million.

VarTec Telecom currently has a \$125,000 performance bond, Excel currently has a \$135,000 performance bond and VarTec Solutions currently has a \$10,000 license and permit bond. The Commission's current bond requirements are \$10,000 for resold long distance, \$25,000 for resold local exchange and \$100,000 for facilities-based local exchange services. Because there will be only one entity remaining at the completion of the transaction, the Applicants have requested that the Commission authorize the cancellation or relinquishment of performance bonds that exceed the Commission's current \$135,000 bond requirement for individual companies providing resold long distance, resold local exchange and facilities-based local exchange services.

Public Interest Considerations

In the application, the parties state that they believe that granting this Application would serve the public interest, convenience and necessity by enabling the seamless continuation of telecommunications services to the VarTec Companies' existing Arizona customers. They also believe that consummation of the transaction will greatly increase the financial viability of the VarTec Companies' products and services and can be expected to serve the public interest by stimulating increased competition in the telecommunications market.

Request for Waiver of Slamming Rules

The VarTec Companies provided notice via first class mail to its customers approximately March 17, 2006. The Applicants have requested a waiver from any applicable anti-slamming regulations that may be considered to have been violated by this transfer of assets being made without the specific authorization and verification of each affected customer. Comtel states that it would be impractical and burdensome to obtain the specific authorization of each customer to effect the proposed transaction and would significantly hinder the smooth transition of services. Staff has reviewed the customer notification letter that VarTec provided to its customers. Because that notice informs customers that the rates, terms and conditions of service will not change as a result of this asset transfer and informs customers that they may subscribe to the telecommunications service provider of their choice, Staff believes the Commission's Slamming and Cramming rules should be waived in this matter.

Recommendations

Staff recommends approval of the acquisition of the VarTec Companies' assets by Comtel. Staff also recommends that Comtel be granted a CC&N to provide resold and facilities based local exchange service and resold interexchange service. Staff also recommends that current VarTec Companies' customers have 90 days following the date of the Commission's order to transfer to another carrier without prejudice or regard to contractual obligation. Staff further recommends approval of Comtel's requested waiver of the Commission's Slamming and Cramming rules in this matter. Staff further recommends cancellation of the VarTec companies CC&Ns to provide telecommunications services in the State of Arizona.

Staff further recommends the following:

1. That the Applicant complies with all Commission Rules, Orders and other requirements relevant to the provision of intrastate telecommunications services;
2. That the Applicant abides by the quality of service standards that were approved by the Commission for Qwest in Docket No. T-01051B-93-0183;
3. That the Applicant be prohibited from barring access to alternative local exchange service providers who wish to serve areas where the Applicant is the only provider of local exchange service facilities;

4. That the Applicant be required to notify the Commission immediately upon changes to the Applicant's name, address or telephone number;
5. That the Applicant cooperate with Commission investigations including, but not limited to customer complaints;
6. That the Applicant offer Caller ID with the capability to toggle between blocking and unblocking the transmission of the telephone number at no charge;
7. That the Applicant offer Last Call Return service that will not return calls to telephone numbers that have the privacy indicator activated; and
8. Staff further recommends that the Commission authorize the Applicant to discount its rates and service charges to the marginal cost of providing the services.

Staff further recommends that the Applicant be ordered to comply with the following. If it does not do so, the Applicant's CC&N shall be null and void after due process. The Applicant shall:

- a. Procure a performance bond equal to \$135,000. The minimum bond amount of \$135,000 should be increased if at any time it would be insufficient to cover advances, deposits, and/or prepayments collected from the Applicant's customers. The bond amount should be increased in increments of \$67,500. This increase should occur when the total amount of the advances, deposits, and prepayments is within \$13,500 of the bond amount.
- b. Docket proof of the performance bond, as a compliance item in this docket, within 365 days of the effective date of an Order in this matter or 30 days prior to the provision of service, whichever comes first. The performance bond must remain in effect until further order of the Commission.
- c. If at some time in the future the Applicant does not collect advances, deposits and/or prepayments from its customers, Staff recommends that the Applicant be allowed to file a request for cancellation of its established performance bond regarding its resold services. Such request must reference the decision in this docket and must explain the Applicant's plans for canceling those portions of the bond.